

New Benchmark Concepts in the GIPS Standards

Fachtag -
Performancemessung und GIPS

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Agenda



- Introduction
- Expanded benchmark description guidance
- Lagged benchmarks
- Custom benchmarks with leverage
- Benchmarks net of transaction costs
- Asset allocation transition
- Actual-weight benchmarks



Introduction

Introduction



- Guidance Statement on Benchmarks for Firms
 - Insight from Exposure Drafts:
 - 2017/2018 Guidance Statement
 - 2020 GIPS Standards
 - Consolidated guidance from:
 - 2020 Provisions
 - 2020 Handbook
 - Relevant Q&As
 - Other benchmark-related guidance
 - Effective 1 April 2021

Introduction



- Guidance Statement on Benchmarks for Asset Owners
 - Insight from Exposure Drafts
 - 2022 Guidance Statement
 - 2020 GIPS Standards Exposure Draft
 - Based on Benchmark Guidance Statement for Firms
 - Tailored for asset owners
 - Consolidated guidance from:
 - 2020 Provisions
 - 2020 Handbook
 - Relevant Q&As
 - Other benchmark-related guidance
 - Effective 30 June 2023

Benchmark Description

Benchmark Description



- Required to disclose a benchmark description in each GIPS Report and GIPS Asset Owner Report
 - General information regarding the investments, structure, and characteristics of the benchmark
 - Must include key features of the benchmark
 - Name suffices for widely recognized benchmark
- Includes many benchmark description examples

Benchmark Description



- Expanded benchmark description guidance includes:
 - Whether the peer group benchmark is gross or net of fees
 - Fixed income characteristics such as duration, credit quality, and yield
 - Currency hedging
 - If a hedged or partially hedged benchmark is used, the hedging criteria for the benchmark
 - Material differences between the benchmark and the pooled fund, composite, or total fund's investment mandate, objective, or strategy
 - If the hedging criteria of the total fund or composite materially differ from the benchmark, should disclose this fact

Lagged Benchmarks

Lagged Benchmarks



- Private market investment valuations are often lagged
 - Benchmark timing should be the same
- If appropriate asset class benchmark is not available on a timely basis:
 - May choose not to include that asset class benchmark
 - Must disclose why no benchmark is presented
 - May choose to use actual return or target return of that asset class when calculating the multi-asset class benchmark return
 - Must disclose this fact

Lagged Benchmarks



- May label benchmark returns as preliminary
 - Update GIPS Report or GIPS Asset Owner Report when benchmark returns are available
 - Subsequently updating the benchmark is not an error
 - Treated in the same manner as an error

Lagged Benchmarks Example

Multi-asset class portfolio performance

- Combined asset class performance = 30 June
- Equity performance = 30 June
- Fixed income performance = 30 June
- Private equity performance = 31 March
- Disclose that there is a difference in valuation dates for the portfolio's private equity asset class

Multi-asset class benchmark performance

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Custom Benchmark with Leverage

Custom Benchmarks with Leverage



- If the composite, pooled fund, or total fund includes leverage, may build leverage into the benchmark
- When leverage is embedded within the expectations of the investment strategy, may determine it is appropriate to use a levered benchmark
- Should systematically incorporate into the benchmark:
 - Additional asset exposure
 - Cost to finance that additional exposure

Custom Benchmarks with Leverage



- Cost of financing is expected to be part of the custom benchmark calculation methodology disclosure
 - When using derivatives:
 - May be more challenging to isolate the cost of financing
 - Should attempt to determine the cost of financing and disclose this amount
- An unlevered benchmark should be presented alongside the custom benchmark with leverage
- Two examples of how to calculate custom benchmarks with leverage

Benchmarks Net of Transaction Costs

Benchmarks Net of Transaction Costs



- Benchmark total returns reduced by transaction costs may be presented
- Transaction costs are typically:
 - Brokerage commissions
 - Exchange fees and/or taxes
 - Bid–offer spreads from internal or external brokers

Benchmarks Net of Transaction Costs



- The benchmark description should:
 - Include the fact that benchmark returns reflect the deduction of transaction costs
 - Identify for which periods transaction costs are deducted
- If a benchmark changes from not deducting transaction costs to deducting transaction costs on a prospective basis:
 - A new return calculation approach is a prospective benchmark change
 - Date and description of the prospective benchmark change must be disclosed for as long as the GIPS Report or GIPS Asset Owner Report includes returns for the prior benchmark
- Benchmark returns should be labeled to make clear that returns are reduced by transaction costs

Asset Allocation Transition

Asset Allocation Transition



- Asset owners typically transition from one strategic asset allocation to another over a long time period.
 - Usually over a predefined transition schedule
 - Will reach the target policy benchmark allocation by a predefined date.
- When transitioning from one asset allocation to another, asset owners may wish to calculate a benchmark that reduces tracking error during rebalancing
 - Between the pooled fund, composite, or total fund and the benchmark
 - Should be done using a predefined schedule
 - Asset owner will change weightings on a predefined schedule (e.g., monthly or quarterly)

Asset Allocation Transition



- Asset Allocation Transition Example:
 - Total fund's hedge fund asset allocation is currently 15%
 - Increase the allocation to hedge funds by 1% each month until reaching the 20% target
 - Increase allocation to hedge funds in the benchmark by 1% each month until reaching the 20% target policy for hedge funds in the benchmark (i.e., strategic benchmark)
 - Rebalancing would be included as part of the custom benchmark description, which includes the benchmark components, weights, and rebalancing process

Actual-Weight Benchmark

Actual-Weight Benchmark



- In most cases the strategic-weight benchmark is the appropriate benchmark
 - There may be cases when it is appropriate to present an actual-weight benchmark
- Actual-weight benchmarks are not commonly used for firms
- When actual-weight benchmarks are used, the strategic-weight benchmark should also be included in the GIPS Report or GIPS Asset Owner Report alongside the actual-weight benchmark

Actual-weight Benchmark



- An actual-weight benchmark should be treated similar to a portfolio-weighted custom benchmark
 - Weights disclosed as of the most recent annual period end
 - Offer to provide information about benchmark weights for prior periods
- Must disclose that the benchmark reflects actual weights rather than strategic weights
- Benchmark description should include the fact that the actual-weight benchmark eliminates the impact of asset allocation decisions
- Decision to use actual weights, the benchmark components, the rebalancing schedule, and rebalancing methodology should be determined in advance

Actual-weight Benchmark



- The term “actual-weight” should be used in the name of the benchmark to indicate it is a custom benchmark
- Details about the calculation methodology of the benchmark must be disclosed
 - Expected to include the frequency of calculation

Questions?



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